



EquityCompass

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Commentary &
Outlook

How to Invest in "If"



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How to Invest in "If" 2025 Second Quarter Commentary and Outlook

Commentary

"If" is not a stock, bond, or mutual fund. "If" is a situation—an economic possibility—that could impact security prices.

Those possibilities are not hard to identify—the financial media keeps a running tab of worrisome likelihoods. However, the challenge for many is not in identifying an "If," but determining what subsequent investment action to take.

For example:

If the economy falls into a recession causing a bear market, how should I invest?

If the economy slows with inflation rising, what's the best strategy for stagflation?

When confronted with uncertainty, despite the lack of science to predict the near-term behavior of complex adaptive systems—namely, the economy and the stock market—investors may choose to reposition their portfolios in an attempt to hedge against possible bumps. Even so, over the years, our observation has been that successful portfolio management has less to do with trying to forecast the unforeseeable and more to do with holding onto solid investments in pursuit of one's long-term objectives.

We believe the best approach to navigating a market full of "ifs" is to "keep a stiff upper lip"—in other words, show courage in the face of adversity. By now, perhaps a few readers have made the connection between the title of this commentary and one of the United Kingdom's favorite poems, "If," by Rudyard Kipling.

The poem is a tribute to Leander Starr Jameson, an English nobleman, who led a raid in 1895 against the Boers in South Africa. Although the "Jameson Raid" was a military defeat, Jameson became a British hero for his courage in leading the attack and then for his willingness to take responsibility for the failed mission. In all,

Jameson's exploits aroused enormous patriotic fervor in England, the likes of which motivated Kipling, a Nobel Laureate, to write his famous poem.

"If" relates the challenges and conditions one must overcome to succeed in life. The question is whether the poem has any important lessons for investors. According to Warren Buffett, the answer is definitively, "yes."

In the Berkshire Hathaway Inc. 2017 Annual Report, Buffett explained how market volatility, in the short run, can often obscure the value that is created by compounding growth over the long term. By example, for over 50 years, Berkshire has reinvested its earnings back into the company, which worked to compound its market value thereby becoming a \$1 trillion business. Yet, over this same period, the share price of Berkshire suffered significant drawdowns (**Table 1**).

If that were not enough, Buffett forewarned shareholders that, in the next 50 years, Berkshire could likely experience similar declines. "**No one can tell you when these will happen**," said Buffett. "**The light can at any time go from green to red without pausing at yellow.**"¹

Buffett further wrote, "**When major declines occur, however, they offer extraordinary opportunities to those who are not handicapped... That's the time to heed these lines from Kipling's 'If.'**"²

What are the major investment lessons Buffett discovered in Kipling's poem?

"If you can keep your head when all about you are losing theirs..."

During difficult markets, it is important to remain calm and unemotional in the face of adversity.

(1) Berkshire Hathaway Inc. 2017 Annual Report, p. 10-11.

(2) Ibid.

Berkshire Hathaway Major Stock Dips

Source: Berkshire Hathaway Inc. 2017 Annual Report, page 10

Table 1

Period	High	Low	Berkshire Decrease
1973-1974 Bear Market (March 1973 - January 1975)	\$93	\$38	-59.1%
October 1987 Stock Market Crash (10/2/1987 - 10/27/1987)	\$4,250	\$2,675	-37.1%
Technology Bubble (6/19/1998 - 3/10/2000)	\$80,900	\$41,300	-48.9%
Financial Crisis (9/19/2008 - 3/5/2009)	\$147,000	\$72,400	-50.7%

Paradoxically, by understanding an adverse situation may be temporary, it can also become an opportunity to invest at lower prices but mostly for those who remain level-headed.

"If you can trust yourself when all men doubt you..."

Although bear markets can shake one's confidence, it is the philosophy of self-reliance—steadfast belief in your long-term investment strategy—that can enable an investor to persevere and avoid panic during periods of market decline.

"If you can wait and not be tired by waiting..."

In markets, patience is a scarce resource. And like all scarce resources, they tend to be the most valuable. Research has shown that long-term investing has outperformed most short-term investing approaches.³ As such, the advantage goes to those who buy and hold, not to short-term traders.

To this, we would also include:

"If you can meet with Triumph and Disaster and treat those two impostors just the same..."

This line conveys what we believe likely to be the most profound insight about markets. It was Kipling's opinion that one should treat both situations, "triumph and disaster," with equanimity. *Why?* Because success does not always beget success, nor should failure determine the end of the road but an opportunity to re-evaluate in pursuit of success. That Kipling referred to both triumph and disaster as

"*impostors*" is the recognition that neither condition is permanent. An investment journey does not end with a single victory or failure.

If we take Warren Buffett at his word, that markets unpredictably can go from "green to red," suffice to say, many investors could face difficult periods in the years ahead. Even so, Buffett believes keeping Kipling's poem at the forefront of one's thinking, particularly during difficult markets, can help investors with better decision making.

Outlook

In our last commentary, we described the first quarter of 2025 in Dickensian terms—"It was the best of times, it was the worst of times."

Investors began the year hot off of the presidential election, giddy with excitement over the possibility of lower tax rates and less regulations—with the hope that the combination might help drive stock prices higher. That is exactly what happened. In the first six weeks of the new year, the S&P 500 Index generated a 4.63% total return—a 48% annualized return.⁴ However, despite the outsized stock market returns, the enjoyment was short lived.

In the last six weeks of the first quarter, the S&P 500 Index declined 8.13% on a total return basis, wiping out the year-to-date gains.⁵ By the end of the first quarter, the S&P 500 Index was firmly in correction territory, down 10% from its February high, posting its worst quarterly return since the 2022 bear market.

What was the reason for the reversal? The new administration's campaign promises to initiate

(3) Ganti, Anu; Tim Edwards, Davide Di Goia; Florence Chapman; Nick Dido, "SPIVA 2024 U.S. Scorecard," S&P Dow Jones: A Division of S&P Global. Also see: Martijn Cremers and Ankur Pareek, "Patient Capital Outperformance: The Investment Skill of High Active Share Managers Who Trade Infrequently," Journal of Financial Economics 122, (August 24, 2016), pp. 288-305.

(4) Total return between 12/31/2024 and 2/19/2025.

(5) Total return between 2/20/2025 and 3/31/2025.

tariffs against U.S. trading partners was announced on February 19, imposing stiff taxes on Canadian steel, aluminum, and lumber imports. The trade war had arrived.

The full extent of the global trade war was not fully revealed until after the market close on April 2—referred to as “Liberation Day.” The administration announced nearly 180 countries were now subject to new U.S. tariffs, with 15 countries—our largest trading partners—receiving the most punitive level of reciprocal tariffs.

Within three trading days, between April 3-7, the S&P 500 Index declined 12%, approaching bear market territory—one of the fastest and worst stock selloffs since World War II.

Then, suddenly the market reversed. On April 9, the Dow Jones Industrial Average was up 2,962 points (+7.87%) and the S&P 500 Index gained 474 points (+9.51%), while the NASDAQ Composite increased 1,759 points (+11.53%). In a snap, it was once again “the best of times.”

Why the turnaround? President Trump agreed to pause the “Liberation Day” tariffs for 90 days to allow countries time to negotiate new trade policies. And in doing so, the pause temporarily removed the economic uncertainty that had been overshadowing the market.

During the “worst of times” first quarter, when the overall market was declining, value stocks beat growth stocks while defensive consumer staples outperformed the high-beta technology stocks. Conversely, during the “best of times” second quarter, growth stocks beat value stocks while the rapidly growing technology stocks significantly outperformed the defensive consumer staples stocks.

The speed and magnitude of price changes in the market have been staggering. The “feast or famine” reaction of many stocks is symptomatic of a market that is being dominated by short-term traders who react instantly to changing headlines. These players do not so much own stocks, as they rent them until the next “tweet” suggests it may be time to make another change.

How should long-term investors navigate this highly volatile and unpredictable market? We

believe in the same manner as they initially began to invest: (1) identify long-term investment objectives, (2) construct a diversified portfolio of stocks and bonds in pursuit of long-term goals, and (3) strive to emotionally distance from day-to-day stock market volatility.

In this uncertain market environment, we recommend investors continue to apply a barbell approach to common stock investing, allocating half of the equities to high dividend-paying value stocks balanced by secularly-advantaged growth stocks. In this way, no matter the future direction of the stock market, one’s portfolio should be prudently hedged.

To this balanced equity approach, we also suggest investors include government-backed bonds to supplement current income and help preserve principal. Not only do we believe this portfolio combination is strategically appropriate for long-term investors, but we are also of the opinion that this approach is tactically right sized for 2025.

Once the portfolio allocation is determined, we believe the proper role of the investor is to monitor the markets and resist constantly buying and selling securities based on the latest news.

However, it is significant to note that monitoring the market doesn’t mean making zero changes to one’s portfolio. There are times when it may be justified to rebalance a portfolio in accordance with investment objectives. For example, when growth stocks materially outperform value stocks, it might be prudent to sell a percentage of growth stocks held in a portfolio in favor of value stocks that may be down in price, and vice versa.

Importantly, this is a far different tactic than making a priori decisions to overweight growth or value based on a hunch the environment could soon prefer one or the other. Keep in mind that by repositioning your portfolio, one is not always penalized for doing so; rather, in doing so, we believe one is being thoughtful in how to potentially enhance the portfolio’s future rate of return.

To be clear, the list of market uncertainties is not limited to trade wars, which remain ongoing.

There could also be economic repercussions to the new “One Big Beautiful Bill Act” as well as uncertainty over a potential rise in inflation and debates over the appropriate level of interest rates. In addition, after generating double-digit growth in the first half of the year, S&P 500 earnings growth is now decelerating. To this, we can add the geopolitical conflicts in the Middle East, including the recent bombing of Iran’s nuclear facilities, alongside the continuing Russia-Ukraine war—all of which could impact market returns. No doubt, there are plenty of “ifs” that raise concerns.

What to do?

Years ago, a long-time Berkshire Hathaway shareholder had the opportunity to meet Warren Buffett. He thanked him for making him rich. Buffett smiled back and replied, *“I didn’t make you rich. You didn’t sell.”*⁶

A gentle reminder that *“keeping a stiff upper lip”* may be the most effective portfolio strategy.

Always, our mandate remains the same. We believe if you can answer these two questions —**what do I own** and **why do I own it**—smartly and rationally, the pathway for higher investment returns may be made easier.

(6) This popular Buffett quote has been paraphrased over the years and is often repeated in investing circles and by financial commentators. It summarizes Buffett’s investment strategy of holding for the long-term and avoid selling prematurely.

About EquityCompass



Robert G. Hagstrom, CFA, is Chief Investment Officer of EquityCompass Investment Management, LLC and Senior Portfolio Manager of the Global Leaders Portfolio. He joined EquityCompass in April 2014 and launched the Global Leaders Portfolio in July 2014. Robert was appointed Chief Investment Officer in March 2019.

Robert has more than 40 years of investment experience. Prior to joining EquityCompass, for 14 years he was the Senior Portfolio Manager of the Growth Equity Strategy at Legg Mason Capital Management led by Bill Miller who was the portfolio manager of the Legg Mason Value Trust. Robert received "Honorable Mention" recognition in Morningstar's Domestic-Stock Fund Manager of the Year in 2007 while with Legg Mason.*

Robert is the author of seven investment books including *The New York Times* Best Seller, *The Warren Buffett Way*, widely considered the definitive book on investment approach and strategies of Warren Buffett. The book, now a *Wiley Investment Classics*, has sold over one million copies worldwide and is translated into 18 foreign languages.[§] In addition, Robert wrote *The Warren Buffett Portfolio: Mastering the Power of the Focus Investment Strategy*, the first book to examine concentrated, low-turnover portfolio management. Robert also wrote *Investing: The Last Liberal Art*, a multi-discipline examination of investing and decision making.

Robert earned his Bachelor's and Master's of Arts degrees from Villanova University. He is a Chartered Financial Analyst, a member of the CFA Institute, and the CFA Society of Philadelphia.

* Established in 1988, the Morningstar Fund Manager of the Year award recognizes portfolio managers who demonstrate excellent investment skill and the courage to differ from the consensus to benefit investors. To qualify for the award, managers' funds must have not only posted impressive returns for the year, but the managers also must have a record of delivering outstanding long-term performance and of aligning their interests with shareholders'. The Fund Manager of the Year award winners are chosen based on Morningstar's proprietary research and in-depth evaluation by its fund analysts. For more information about Morningstar Awards, visit <https://go.morningstar.com/Morningstar-Awards>.

§ Source: www.wiley.com

About EquityCompass

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